United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

74-1661

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74-1699
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In The

United States Court of Appeals

For The Second Circuit

FABRIZIO & MARTIN INCORPORATED,
Plaintiff-Appellee-Appellant,

vs.

BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE, NORTH CASTLE AND POUND RIDGE, MARS ASSOCIATES, INC., and NORMEL CONSTRUCTION CORP. OF NEW ROCHELLE, a joint venture,
Defendants,

THE BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE, NORTH CASTLE AND POUND RIDGE,
Defendants-Appellants-Appellees,

AETNA CASUALTY & SURETY CO., Additional Defendant on the Counterclaim of Defendant Board of Education,
Defendant-Appellee-Appellant.

On Appeal from a Judgment of the United States District Court for the Southern District

ARGUMENT FOR THE BOARD OF EDUCATION IN REPLY TO BRIEF FOR AETNA CASUALTY & SURETY CO.

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ARGUMENT FOR THE BOARD OF EDUCATION IN REPLY TO BRIEF FOR AETNA CASUALTY & SURETY CO.

POINT I

AETNA IS LIABLE FOR ANY JUDGMENT AGAINST FABRIZIO

In POINT I of its brief, AETNA claims that vis-a-vis the BOARD and AETNA, the equities were in AETNA's favor and that therefore AETNA is not liable on its performance bond.

AETNA's disclaimer of liability is based on its claim that the BOARD fraudulently withheld and concealed information from it and that the BOARD fraudulently induced FABRIZIO to enter into an illegal contract.

That FABRIZIO was not the innocent contractor as portrayed by AETNA shall be discussed in a subsequent point.

AETNA's argument that the BOARD committed a fraud which relieves the Surety of its liability is equally unpersuasive.

The BOARD had no obligation to make any disclosure to AETNA. The BOARD did not even know that AETNA was in the picture until after the bond had been executed and delivered. In addition, it had no way of knowing what FABRIZIO had or had not disclosed to AETNA. Certainly AETNA made no effort to find the facts and circumstances of this matter. It did not even require FABRIZIO to supply the basic contract information required on its own application form.

AETNA's own witness paraded to the witness stand one after the other and said that no effort was made to review the contract and that the bond was issued because FABRIZIO was a good customer. (pp. 822a ff).

It is a well-established principle of law that a surety cannot be excused from reasonable attention to the circumstances and reasonable diligence to inform itself as to the prudence of the act it is about to do, 3 A.L.R. 1494.

BOARD did not ask AETNA to provide the surety bonds, nor was it ever asked any questions by AETNA. BOARD directed FABRIZIO to provide surety bonds from anyone it would as surety, and it didn't direct FABRIZIO what information to give or to withhold. AETNA submitted an application form to FABRIZIO, asking questions, most of which were left blank and unanswered. One unanswered question was potentially a key question: it asked who the bidders were and the amount of their bids. Had it been answered, it might have stimulated AETNA into asking pertinent questions. AETNA accepted the application in its unanswered form.

This Court, in the recent case of Mohasco Industries, Inc. v. Giffen Industries, Inc., 335 F. Supp. 493, 496-497, SDNY 1971), ruled in a similar situation as follows:

> "Under New York Law which applies here, it is true that there are circumstances under which the silence of an obligee under a surety contract as to a material fact may constitute a fraud upon the surety and relieve him of liability. Bostwick v. Van Voorhis, 91 N.Y. 353 (1883)

. . . But the mere characterization of silence on the part of the obligee as "fraudulent" does not suffice unless it is shown that there was some duty on the part of the obligee to speak--a duty to disclose a material fact of "so decisive a character that it could not be supposed that if known to the surety he would have entered into the obligation." Howe Machine Co. v. Farrington, supra [82 N.Y. 121, 125]. The failure of an employer to disclose to a surety that an employee whom the surety was bonding had previously been guilty of dishonesty, for example, would amount to a fraudulent concealment and would void the contract of suretyship. Bostwick v. Van Voorhis, supra; Howe Machine Co. v. Farrington, supra.

"In order to constitute fraud, however, silence on the part of the obligee must be tantamount to affirmation of a state of affairs which does not exist and which would have the effect of deceiving or defrauding the surety. The obligee is not under an obligation to disclose to a surety information of which the surety had knowledge readily to hand. A surety cannot rest supinely, close his eyes, and fail to seek important information and then seek to avoid liability under the guaranty by claiming he was not supplied with such information. Magee v. Manhattan Life Insurance Co., 92 U.S. 93, 23 L. Ed. 699 (1875). Moreover, as stated in Bostwick v. Van Voorhis, supra:

'...[T]hey [sureties] must inquire and inform themselves of all the facts they desire to know, and if they omit to seek for or obtain the requisite information, they cannot easily avoid the bond upon inferential or unsatisfactory proof that they were drawn into signing it by bad faith on the part of the obligee. Before a bond in such a case can be avoided, the fraud and bad faith should be brought home to the obligee by quite clear and decisive evidence, otherwise bonds of this character will furnish a very precarious security to the parties who take them.' (91 N.Y. at 360-361)" (emphasis added).

See also Howe Mach. Co. v. Farrington, 82 N.Y. 121 (1880), and 3 A.L.R. 1494.

No evidence was introduced that BOARD knew at the time that it

entered into the FABRIZIO contract, it was doing so in violation of statute. To the contrary, the proof is that BOARD acted in reliance upon advice from its attorney, and therefore assumed that what it was doing was proper. It cannot be aid, therefore, that BOARD failed to tell AETNA of the circumstances with intent to deceive it. Such knowledge and intent cannot be presumed, and must be proven. In actions for deceit, the presumption is in favor of innocence and the intent or design to deceive must be affirmatively made out by evidence. Wakeman v. Dalley, 51 N.Y. 27.

BOARD could not inform AETNA that the contract was illegal until Judge McLean's decision declared it illegal. Until that moment it took the position that the contract was legal (as did FABRIZIO), and strenuously litigated that position. BOARD took that position although at that time the law was that it would have been entitled to the return of the entire $2,100,000 already paid FABRIZIO. In order to hold BOARD for concealment, AETNA must affirmatively prove that it relief upon BOARD. It had no dealings with BOARD of any kind prior to the execution of the bond and no such proof has been offered. If anything, AETNA offered proof it relied upon only FABRIZIO. First Citizens Bank & T. Co. v. Sherman's Estate, 250 App. Div. 359.

AETNA did not even have a representative at the contract closing. If it had, it would have seen the typewritten change order annexed to the printed contract. The fact is that AETNA never attempted to obtain the facts, and therefore may not now disclaim liability. Hartford Acc & Ind. Co. v. Kranz, 7 A.D. 2d 604 (3rd Dept. 1959).

The Court below was correct in holding that the BOARD's action did not constitute fraud. As the Court found:

> "The Board did not ask Aetna to provide the surety bonds, nor was it ever asked any question by Aetna. The Board directed Fabrizio to provide surety bonds and Aetna submitted an application to Fabrizio, asking some questions which were never answered. Aetna made little effort to discover the facts and circumstances surrounding the illegal contract, but rather appeared to rely on the fact that Fabrizio was a good customer. Moreover, the evidence does not indicate that the Board knew that the contract was a violation of law. To the contrary, the proof is that the Board acted in reliance upon advice from its attorneys and assumed that it was acting properly. At best the Board's knowledge of illegality was equivocal, making failure to disclose it insufficient to establish fraud." (1072a)

Those were the findings of fact in the District Court and refute AETNA's contention that there was fraud on the part of the BOARD and that vis-a-vis the BOARD and AETNA, the equities were in AETNA's favor.

Finally, AETNA contends that an innocent Surety is not liable on its performance bond. As stated, the District Court found AETNA not to be at "innocent" as it contends. Moreover, both of the law of the State of New York and the law of this case make it clear that AETNA is liable on its performance bond.

In support of its position, AETNA cites as its main authority for that purpose the case of Village of Medina v. Title Guaranty & Surety Co. of

Scranton, Pa., 152 A.D. 308, 136 N.Y. Supp. 786 (4th Dept. 1912). In its decision reversing a summary judgment in favor of AETNA in this very case, the Circuit Court of Appeals rejected the Medina case as being inapplicable to the instant case.

AETNA further cites Pittsburgh Construction Co. v. West Side Belt Co., 154 F. 929 (3rd Cir. 1933) is not applicable to this case. It merely held that an action brought in Federal Court could not be maintained by a foreign corporation not qualified to do business in the State of Pennsylvania.

A subsequent action between the same parties was instituted in the Pennsylvania State courts which eventually went to the Supreme Court of the United States (West Side Belt Co. v. Pittsburgh Construction Co., 219 U.S. 92, 55 L. ed. 107). In the second case, the decision in the first action was put forth as a defense, and that defense was rejected on the grounds that the Federal action had settled nothing with respect to the merits of the case. The Court said that the only issue adjusted was plaintiff's right to maintain its action as an unregistered foreign corporation.

If anything, Pittsburgh is analogous to what has happened in BOARD's action against AETNA. As the Circuit Court of Appeals said in the instant case, in Judge Moore's opinion:

> "As noted, the Board's complaint was dismissed on Aetna's motion for summary judgment on the theory that Aetna's surety was absolved of all liability because the construction contract was invalid. This ruling is at issue here."

Judge Moore then pointed out that the District Court had relied, for New York law, on Medina, and Kent v. Thornton, 179 Misc. 593, aff'd 265 A.D. 904, and decisions of courts in other States. The lower court had rejected Gerzof because the Gerzof theory of liability did not affect AETNA, as surety, in any way.

But Judge Moore said that the Gerzof approach is justified in this case. "In Gerzof the wrong was done to the Village of Freeport by the connivance of Nordberg and the Village officials; in our case, to the taxpayers, by the connivance of FABRIZIO and BOARD." After reviewing Judge Ryan's holding in the FABRIZIO case, Judge Moore stated:

> "In other words, until a judgment, if any, is rendered for damages, if any, against Fabrizio and in favor of the Board, there is no way of determining whether the condition of the surety bond has been met. It is abundantly clear from Judge Ryan's decision that he did not hold that Fabrizio could not under any circumstances be liable to the Board for damages. Damages could only have been incurred in connection with the construction of the school and it was for proper performance of this construction work that Aetna stood surety. Nor did the Judge hold that the Board's counterclaims must be dismissed although the contract's invalidity prevented Fabrizio from recovering. He held quite to the contrary. Had the invalidity of the contract prevented the Board from obtaining any recovery for damages against Fabrizio, Aetna's contention might have greater merit."

Judge Moore further stated:

> "Although this decision removes Aetna's premise of no liability under a void contract, it does not establish the nature or extent of the damages, if any, recoverable by the Board against Aetna. Such a determination can only be made after full development of the fact relating to the underlying equities, vis-a-vis the Board and Aetna."

What Judge Moore found, in effect, is that in this type of case, illegality is the shield of the public agency and the sword of the public. That is the real meaning of Gerzof.

If the Court does not grant damages to BOARD, FABRIZIO and AETNA will be receiving indirectly the benefit of a quantum meruit recovery, despite Judge Ryan's prohibition.

AETNA guaranteed FABRIZIO's performance. It is bound to its guarantee. That it never read the contract is no excuse.

The bonding company is the alter ego of the contractor. One of the elements required by the competitive bidding statute is that the successful contractor be "responsible". A test of responsibility is whether or not the contractor is bondable. If FABRIZIO were not bondable and had not produced a bond, he could not have received the contract.

AETNA's bond is the equivalent of a cash deposit to make good for the contractor's inability to do so. BOARD is not suing FABRIZIO and AETNA for different sums. It is suing them both individually and jointly for the same damages, so that if FABRIZIO does not pay, its surety will.

AETNA is a compensated surety that agreed to make good for any deficiencies or defaults in FABRIZIO's performance. All BOARD seeks now of AETNA is that it be held to its promise to make good for FABRIZIO. This means

that to the extent that there is a judgment against FABRIZIO arising out of the illegality of the contract, AETNA must also be held liable.

The purpose of AETNA's bond, like that of every bond, is to ensure payment if the principal cannot pay. The basic rationale of this action in its present posture is to preserve the sanctity of the competitive bidding statutes and thereby to protect the public interest. Recovery of damages is the technique that the Court of Appeals in Gerzof, supra, Albany, supra, and the long line of New York cases, has determined as the most fruitful way of preserving the sanctity of the statute.

The essence of the illegality of the FABRIZIO contract was that the public got $171,000 less in value than it voted for in its bond issue. It would be a mockery of the principle of both Gerzof and Albany, to hold that the public could have gotten that $171,000 in value, as AETNA and FABRIZIO claim, by paying almost $300,000 more to the third lowest bidder.

That there was the $171,000 change order did not materially increase the risk that the surety assumed in the usual course of its business in insuring the performance of a contract. AETNA's bond agreed that if FABRIZIO did not perform the work, AETNA would arrange to complete the work. The Change Order did not make FABRIZIO's performance of the work either impossible or more difficult. As event turned out, the courts held that it was in violation of the com-

petitive bidding statutes. But this did not affect FABRIZIO's ability to perform the contract. Thus, it did not affect AETNA's risk under what AETNA agreed to do.

Actually, there was no non-disclosure of the Change Order. It was physically attached to the original contract and made a part of it and signed by FABRIZIO and BOARD's president, rather than by the architect, as was the case in all other Change Orders, and had AETNA ever asked for the contract or sent a representative to the contract closing, it would have observed the typewritten Change Order physically attached to the printed contract, and had the opportunity to raise questions about it. Had this occurred and had BOARD then failed to make disclosure, there might be warrant for AETNA's position, but none of that occurred. AETNA suffered itself to become "an indolent victim". It is to be construed that AETNA should have known of the change order. (5711 G. Juris, Suretyship and Guaranty Sec. 594).

AETNA knew what it was insuring and at no time attempted to disclaim liability and return the premium. It cannot, and should not, be released now. Hendrie v. Board of Cty. Comrs., 387 P. 2d 266, 1 A.L.R. 3rd 86'.

The measure of liability of a surety on a bond is coextensive with the liability of the surety's principal. Eckstein v. Massachusetts Bonding and Insurance Co., 281 N.Y. 435, 440 (1939); Levie v. Cottage Homes, Inc. 124 N.Y.S.

2d 118 (Sup. Nassau 1953); Matter of U.S. v. Century Indemnity Co., 282 N.Y. 95 (1940). Such liability of the surety does not therefore depend upon the illegal contract, but rather on the damages for which its principal is responsible. 50 Am. Jur. Suretyship Sec. 148.

The competitive bidding statutes were enacted for the purposes of protecting governmental bodies from improper purchasing methods conducive to unreasonable prices, poor quality and possible collusion between public officials and private companies. AETNA seeks to absolve itself of liability because of the non-compliance with the competitive bidding requirements, with the untoward result of causing serious harm to the BOARD, the antithesis to the purposes of such statutes. The defense of illegality of a contract is allowed not as a protection to a defendant, but as a disability to plaintiffs. 10 N.Y. Juris. Contracts Sec. 176. In the within action, the contract between FABRIZIO and the BOARD was declared illegal to protect the public interest, and not to shield surety companies. In such instance, the BOARD is not regarded as in pari delicto. 10 N.Y. Juris. Contracts Sec. 181; 120 A.L.R. 1461.

In the cases of Ring v. Gibbs, 26 Wend (N.Y.) 502, 505 (1841) and Mundorff v. Wangler, 12 Jones & S. (N.Y.) 495, 505 (1879), it was held that a surety would not be discharged from liability because of the illegality of a contract flowing from a failure to comply with statutory provisions enacted for the protection of the public or a particular group.

POINT II

THE BOARD COMMITTED NO FRAUD UPON AETNA WHICH WOULD ENTITLE AETNA TO DAMAGES

As set forth in POINT I of this reply, the facts in this matter and the findings of the Court below clearly indicated that there was no fraud committed upon AETNA by the BOARD.

AETNA relies upon Damon v. Empire State Surety Co., 161 App. Div. 875 (1940). The factual situations in Damon were unusual and entirely inapplicable to this case. There was proof in Damon of a conspiracy to defraud the surety. The alleged "new" contract was, in fact, an extension of the existing contract already in default. No such factual situation occurred in this case.

AETNA also relies upon Bank v. Board of Education of the City of New York, 305 N.Y. 119, which is inapplicable.

In Bank v. Board, judgment was awarded an electrical contracting firm against the Board of Education of the City of New York on the ground that plaintiff's were induced to contract with the Board to install electrical fixtures in a proposed addition to a school building by the Board's implied representation that it was simultaneously awarding to other bidders a plumbing contract and heating contract and that the Board accepted plaintiff's bid and required plaintiff to sign a contract without notifying plaintiff that it had decided to postpone

the award of plumbing and heating contracts until more money might become available in the next fiscal year. It was found that the resulting interruption and delays in the work caused plaintiff $16,000 in labor and material.

In Bank v. Board, unlike the instant action, the electrical company entered into a contract with the City. In the instant action, the BOARD did not ask AETNA to provide the surety bonds, nor did BOARD even know that AETNA was in the picture until after the bond had been executed and delivered.

Additionally, in Bank v. Board, Board was aware that it would not intend to award plumbing and heating contracts prior to entering into its contract with the electrical companies and failed to notify the electrical companies of this fact. The BOARD in the instant action did not know that the contract between the BOARD and FABRIZIO was entered into in violation of the public bidding statutes at the time it entered into its contract with FABRIZIO and at the time AETNA agreed to provide the surety bond.

There was, in fact, no fraud committed upon AETNA by the BOARD which would entitle AETNA to the recovery of damages.

POINT III

THE BOARD IS ENTITLED TO RECOVER ALL OF THE DAMAGE IT SUFFERED AS A DIRECT CONSEQUENCE OF THE ILLEGAL CONTRACT, INCLUDING BUT NOT LIMITED TO THE ITEMS ENUMERATED BY THE COURT OF APPEALS IN GERZOF.

In POINT III(a) of its brief, AETNA takes the position that the damages sought by the BOARD are not the result of the illegal contract and therefore not recoverable in this action.

The salutary rationale and policy underlying Gerzof and preceding and subsequent decisions is that, as a matter of public policy, the public may suffer no damages as a result of the illegal contract. The public must be made whole in every way and the public treasury protected.

The damages which must be ascertained and proven are the BOARD'S actual loss, not reasonableness of loss, nor value of services, or any other measure of damages normally used in breach of contract actions. As stated in POINT II of BOARD's main brief, the $280,796.00 sought by the BOARD for completion costs, which include $165,430.00 as "increased completion costs" and $115,366.00 for 30 years' interest are damages which could only have occurred in connection with the construction of the school and under the Ryan decision and Gerzof guidelines are damages which could only have occurred as a direct result of the illegal contract.

Despite the claim made by AETNA (Aetna's brief, page 48), the BOARD has produced sufficient evidence to substantiate its claim to this sum.

As stated in Gerzof and applied to this case by Judge Ryan, the BOARD need only prove its actual loss, not reasonableness of loss or value of services.

As stated in POINT II of BOARD's main brief (pp. 28-31) the Court below recognized the applicability of this rule and determined that the BOARD can talk in terms of "costs" and not in terms of the value of services performed to prove damages. To substantiate these claims as to the "actual cost of completion", BOARD adduced testimony that this was indeed the actual cost to the BOARD of completing the school.

The testimony of Mr. Fowler and Mr. Crane, which is uncontroverted, clearly indicates that the amount demanded by the BOARD represents the "additional cost of completion" of the school. (See BOARD's main brief, pp. 28-31 for discussion of the testimony of Fowler and Crane.)

Therefore, based upon the Gerzof decision, the law of this case as set forth by Judge Ryan, and the measure of damages as recognized by this Court, the defendant has proven its claim to damages. The BOARD has shown that its "actual loss" was in relation to the "cost of completion" of the school.

The BOARD's evidence is uncontroverted and it need prove no more.

However, even if the rule as set down in Gerzof were deemed not applicable in determining whether the BOARD has substantiated its claim to damages, the BOARD has adduced sufficient evidence to support its claims.

In asserting that the BOARD failed to sustain its claim for damages, AETNA takes the position that because the BOARD did not introduce the contracts of Mars-Normel, Broadhurst and MacNamee into evidence, the BOARD was barred by the best evidence rule from testifying as to the cost of completion. They also contend that the BOARD's Exhibits 85A to 90F (D 58-87R) were introduced into evidence subject to verification which was never produced.

As a matter of law, its position must fall.

The best evidence rule applies exclusively to documentary evidence, the contents of which are in issue. A party attempting to prove a fact contained in a written instrument must produce that instrument. However, the best evidence rule does not apply to writings which are collateral, i.e. incidental to

proving the issues in dispute. United States v. Aluminum Co. of America, 35 F. Supp. 820 (S.D., N.Y. 1940); Daniels v. Smith, 130 N.Y. 696 (1892). Moreover, if the facts to be proven exist independently of the document, the facts may be proven without resorting to the original document. Harmon v. Matthews, 27 N.Y.S. 2d 656. See also Herzog v. Swift & Co., 146 F. 2d 444 (2nd Cir. 1945).

In the instant action recovery is not sought on the completion contracts themselves. The facts to be proven here are not the terms of the contracts between BOARD and Mars-Normel, Broadhurst and MacNamee, but the damages suffered by the BOARD because of FABRIZIO's failure to complete the school. The best evidence of the damages to the BOARD is the requisitions for payment and proof of payment which have been submitted.

Furthermore, neither AETNA nor FABRIZIO objected at the trial to the failure to submit the above mentioned contracts and cannot do so now. (Civil Practice Law and Rules, Sec. 4017). The objection, like an exception, should have been made at the trial, and then at the earliest possible moment. Two reasons are given in Weinstein, Korn and Miller, New York Civil Practice, Sec. 4017.03. The first is to give the court and the opposing party the opportunity to correct the error at the earliest opportunity. The second is that it is "basically unfair" to wait until one sees the effect of waiting. AETNA is therefore precluded from making this objection now.

As to the allegation that the BOARD failed to submit "back-up" verification to its Exhibits 85A through 90F, and was thus precluded from claiming payments to Mars-Normel, Broadhurst and MacNamee, it is submitted that the BOARD did supply adequate back-up to permit this Court to consider its claims for payment to them. In its Exhibits 85A to 90F, the BOARD submitted these contractors' requisitions for payment for work done for the completion of the Middle School construction. These requisitions were accompanied by claim forms, additional summaries of the work done, and certifications of the architect.

This Court, in allowing these exhibits into evidence, did so with the proviso "that Mr. Yavner is going to have to produce the architect ... or the back-up material in order to enable the plaintiff and the defendant to cross-examine as to whether the money was in fact paid and for what." (p. 333a) Accordingly, Exhibits D99-130R were introduced by the BOARD as its back-up; they contain, in addition to the material submitted in Exhibits 85A to 90F, check copies showing payment for the amounts of the requisitions, invoices for materials produced and other back-up documentation.

The BOARD has therefore shown that the money was "in fact" paid. Additionally, Mr. Yavner also "produced" the architect, as required by the Court, who testified as to what the money was paid for. Mr. Crane stated, in regard to Exhibits D99-130R, that he had examined the requisitions and the

back-up documents when originally submitted and verified that the work was done (p. 750a). The requisitions attached to these exhibits bear his initials, as well as those of the BOARD's Clerk of the works (p. 751a).

Crane further stated that he was able to verify that the work done was the responsibility of FABRIZIO (p. 757a).

Moreover, although Mr. Powers called these records "just summaries" (p. 323a), Exhibits D58-87R and D99-130R are more than summaries; they contain original documentation of the claims. But even if they were "summaries", they are sufficient in law to establish the amount of damages to BOARD, as shown below.

Brandes testified (pp. 1013a, et seq.,) that he prepared the requisitions and claim orders in the "normal course of work"; that he visited the job site every other day for a half-day, reviewed the progress with the superintendent, reviewed the manpower required, the sequence of operations, and the preparation of all papers and documents, and that, based upon the time and material slips - prepared every day by the superintendent on the job site and checked and signed by the BOARD's Clerk of the Works, he, Brandes, would prepare the monthly requisition and summary of work done.

Crane certified that the requisitions and summaries for the work of Broadhurst and MacNamee were also prepared in summary, based upon the time

and material slips and other back-up which he, as architect, verified.

It is a well established rule of law that such summaries, as well as the records from which they are made, are records made in the regular course of business, admissible as such, and sufficient to establish a claim for the amount of charges contained therein.

In Erecto Corp. v. State, 29 A.D. 2d 728, 286 N.Y.S. 2d 562 (App. Div. 3rd Dept. 1968), claimant sued to recover on a contract for construction of traffic signs. The State had deducted $5,639.21 from the monies paid contractor as engineering charges because the job had not been completed on the date specified in the contract.

Claimant contended that the State failed to prove that the sum deducted actually represented the engineering and inspection expenses incurred by it. At the trial, the State had introduced in evidence a summary of the engineering charges deducted, which summary was prepared from a record of the days and hours and personnel used at the job site which the State requested its engineer to make.

The Court held:

> "This summary, as well as the records from which it was made, were records made in the regular course of business of the State and were properly admitted into evidence. (CPLR 4518, subd. [a].) This was the only evidence of the amount of the charges, and it stands uncontradicted. It was, therefore, sufficient to establish the amount of charges."

In Connecticut Importing Co. v. Frankfort Distilleries, 101 F. 2d 79 (2d Cir. 1939), plaintiff, a liquor distributor, sued for treble damages because his supply had been cut off for violating price maintenance agreement. Over defendants' objection, he introduced proof of damages through testimony of a certified public accountant of a computation he had made from plaintiff's books of account. The Court ruled that this was competent evidence, stating, "If the computation was incorrect, it was subject to being overcome by proof to that effect." See also Wm. H. Rankin Co. v. Eastern Bill Posters of U.S., etc., 42 F. 2d 152, 155 (2d Cir. 1930).

In the instant action, the BOARD's architect, Crane, showed damages by computations made from the contracts between the BOARD and FABRIZIO and the requisitions of Mars-Normel, Broadhurst and MacNamee, which evidence was not overcome by proof.

In Youngs Drug Products Corp. v. Dean Rubber Mfg. Co., 362 F. 2d 129 (7th Cir. 1966), plaintiff sued for a judgment for unfair competition. The Court said:

> "The only proof of damages was by documentary summaries or damage schedules prepared primarily from monthly operating statements or summaries. Dean argues this evidence was inadmissible as violating the best evidence rule. It claims also that it was denied the opportunity to inspect the original records and to cross-examine with respect to the occuracy of the underlying 'work sheets'."

In review the objection of Dean to the admissibility of this evidence, the Court stated, at p. 134 :

> "We see no merit in Dean's contention. The preparation of the damage summaries was shown by the witness who prepared the exhibit to have been from audited monthly statements made from records kept in the regular course of business. He was subjected to extensive cross-examination. Youngs' comptroller, who assisted the accountants in completing the audit and preparing the statements, testified and was cross-examined. The statements were used in regular course for declaration of dividends, annual reports and federal income tax returns. The statements underlying the damage summaries were introduced for use in cross-examination by a co-defendant of Dean without objection by the latter. We conclude that the documentary summary entitled 'Computation of Shipments Lost, 1958' was admissible as a summary of transactions, constructed from monthly statements made in the regular course of Youngs' business. 28 U.S.C. § 1732. The district court could properly infer that the statements were made within a month after the transactions and therefore 'within a reasonable time', and that on the whole there was sufficient verification of the statements and the 'Computation'."

In the instant action, a portion of BOARD's proof of damages was documented summaries prepared monthly (a period of time found not to be unreasonable by the court in Youngs) from statements (time and material slips) which had been prepared daily in the regular course of business, it being the

regular course of such business to make such memoranda. (Brandes, pp. 1013a et seq.)

As in Youngs, AETNA and FABRIZIO claim they were denied the opportunity to cross-examine with respect to the accuracy of the underlying time and material slips (work sheets). Actually, the material slips are attached, although time slips are not attached to Mars-Normel requisitions, but are attached to Broadhurst and MacNamee requisitions.

As in Youngs, there is no merit to the AETNA-FABRIZIO contentions. As in Youngs, the preparation of the requisitions and summary were prepared monthly from records kept in the regular course of business. Brandes, who prepared the requisitions and summary, could have been subject to cross-examination, but, on objection sustained by the Court, was dismissed from the stand.

The underlying time slips, although not introduced into evidence, were produced at trial and marked for identification as Exhibit 125, and could have been used to cross-examine Crane and Brandes.

Therefore, as in Youngs, these "summaries" were sufficient proof of BOARD's damages.

See also: Peter Kiewit Sons' Co. v. Summit Construction Co., 422 F. 2d 242 (8th Cir. 1969)

In the instant action, the "summaries" were prepared in the regular course of business as summaries of other records still existing and kept in the

regular course of business such as time and material slips. Similar summaries of proper business records have often been accepted into evidence.

Furthermore, here, as in Kiewit, supra, and as in Hotovec v. Howe, 79 D.S. 337, 111 N.W. 2d 748, 749-50 (1961), the actual records were in the courtroom, available to the plaintiff and additional defendant for inspection and had been offered in evidence through Mr. Brandes (p. 1013a et seq.).

These records should have been accepted in evidence pursuant to 28 U.S.C.A., Section 1732, entitled "Record made in regular course of business; photographic copies", and Section 4518(a) of the CPLR, entitled "Business records".

The measure of damages is not the difference between the next lowest bidder and FABRIZIO's bid, as is suggested in FABRIZIO's brief (p. 60), but the difference between the actual cost to the public of the work submitted in the original plans and specifications and the original bid of FABRIZIO in the sum of $2,326,900.00. Only by assessing such damages will the public be made whole, the prime directive of Gerzof; only by assessing such damages will the New York rule that the public must not be damaged by the illegal contract be complied with.

Despite AETNA's contention (Aetna's brief, p. 61) that even if the Change Order of $171,000 was added to FABRIZIO's bid, the BOARD would still

have been required to pay an additional $51,100.00, as Judge McLean said in his opinion (94a):

> "The work that Fabrizio was called upon to perform was different from that which all other contractors were asked to bid on. No one can say with certainty that if these modified plans had been made available to all would be bidders, one of them would have bid a lower figure than Fabrizio's $2,326,900.00. On the other hand, no one can say with certainty that this would not have occurred. The intent of the statute is that all bidders are entitled to an equal opportunity."

If there is any speculation as to whether and to what extent the alternate plans would have produced savings to the public, such speculation must be resolved in favor of the public so that it may not be harmed by the illegal contract and so that the sanctity of the bidding statutes are preserved.

In addition, the sum of $708,526.15 which AETNA claims the BOARD has successfully avoided paying to FABRIZIO for services, labor and materials was never substantiated. As a matter of fact, there was no evidence introduced at the trial to show the value of the alleged unpaid for services, labor and materials received by the BOARD. As a matter of fact, the Court specifically excluded any evidence as to the value of the unpaid for services, labor and materials allegedly supplied by plaintiff to the BOARD, for which plaintiff seeks recovery of $708,526.15.

POINT IV

FABRIZIO IS NOT THE INNOCENT VICTIM HE IS DEPICTED TO BE IN AETNA'S BRIEF.

In its brief (p. 63) AETNA states:

> "The Board never advised Fabrizio that there were grave questions of legality so that Fabrizio could seek the advice of counsel. Instead, the Board entrapped Fabrizio into thinking everything was legal and proper."

Although the transcript of the hearings held by Judge McLean is not in the record of this appeal, the decision recites enough detail to make clear that Fabrizio was an active participant and negotiator in the illegal bidding process. On February 10, 1964 Fabrizio met with four members of the then Board, the Board's then attorney and a representative of the Board's architect. Not only did Judge McLean take testimony about this meeting, but also a tape recording of the meeting was introduced into evidence together with a typed transcript of the recording. Fabrizio was one of the "participants in the meeting", as Judge McLean phrased it, and he and the others together "attempted to find a way" to eliminate $171,000.00 worth of work from the specifications to compensate him for the bidding error he told the Board he had made. Suggestions were made, "but no agreement was reached", except that Fabrizio agreed to "discuss the matter further with the architects".

Obviously, if "no agreement was reached," it was not reached between Fabrizio and the other participants. Was he listening and talking? Obviously. Was he the utter innocent that his Brief describes? Hardly.

Fabrizio could not have been such an innocent, because the tape recording tells what was said in his presence and what he responded. He heard the Board Chairman say to him - not to some mythical person, but to him, Fabrizio:

> "See, we wind ourselves up with the problem that under State law, if we would then take your change of figure here it would then violate the basis upon which we then could grant the contract...there would have to be some way that we could find making this thing up somewhere along the line. Have you got any bright ideas?"

He heard another member spell things out to him in language a contractor understands:

> "I mean, to be utterly blunt about it without saying anything [.] I don't think this si something that would bear repeating...and I think in your mind's eye you have got to go back and look at these contingencies..."

He heard the architect inquire:

> "What would you propose to do then? Enter into the contract without any of this on paper?"

He heard one Board member reply "Oh, no," while another simultaneously said, "You have got to."

And in response to all this, Fabrizio said:

"I would be willing to cooperate as much as you people would like me to."

He "cooperated" with the architect during the next couple of days. They discussed, explored, collaborated and finally agreed on removal of certain items from the base plans to create the $171,000.00 saving that Fabrizio wanted. On February 18th he wrote a letter to the Board that if his firm was awarded the contract "at our bid figures," he would withdraw his request to withdraw his bid; but meanwhile he and the architect had worked out changes as a result of which Judge McLean found, "the net saving to Fabrizio came to $1,677.00 more than the $171,000.00 error." And, on March 17, he signed the construction contract at prices which "were the exact sums" bid on January 7, 1964; but simultaneously he signed a change order which, Judge McLean found, reduced his costs by $172,677.00 and required him to make a cash allowance of $1,677.00 to the Board.

In this recital by Judge McLean consistent with the portrait painted in the Brief of a public works contractor who didn't know what was happening, who was oblivious? Of course not.

Yes, he did hear the question put to the Board's attorney at the February 10th meeting:

"Is this reasonable to do, counsel, without prejudice? We don't expose ourselves to slings and arrows from the other bidders?"

Yes, he did hear the answer:

"No. No exposure."

But Judge McLean's decision does not reveal what Fabrizio thought of this answer; nor does the decision tell, as of course it cannot, for this was not an issue at the hearing, whether Fabrizio consulted with his attorneys during the period from February 10th to March 17th.

There is a finding by Judge McLean that the Board's attorney advised the Superintendent of Schools that although Fabrizio's contract provided for $99,000.00 for Alternate No. 3, on which the bond issue was only $95,000.00:

"Mr. Fabrizio has agreed orally with Mr. Van Allsburg [chairman of the Board] that the certificates covering this work will not exceed $95,000.00 but that this will not affect the total contract price."

It is a fair inference that no experienced public works contractor engages in such a conversation without at least suspecting that there may be a violation of the public bidding laws.

It is not meant by this discussion to charge Fabrizio or the former Board members with fraud or malice, for no one believes there was any.

Judge McLean said specifically:

> "Here the question is not one of fraud, but of illegality."

As Judge McLean reported his findings of fact, it is clear that he found all of the participants, including the Board members and Fabrizio, had committed impropriety, wrongdoing and illegality although not fraud.

Even though both parties may have been innocent of intent to do wrong, the fact found by Judge McLean is that wrong was done, and Fabrizio cannot escape from his participation.

The United States Court of Appeals for the Second Circuit, in the appeal in the case of the Board v. Aetna Casualty & Surety Company (119a) did not view Fabrizio as being entrapped by the Board nor as the total innocent depicted in Aetna's brief. As the Court said (127a):

> "In Gerzof the wrong was done to the Village of Freeport by the connivance of Nordberg and the Village officials; in our case, to the taxpayers, by the connivance of Fabrizio and the Board." (Emphasis added)

Moreover, AETNA's brief misinterprets the Gerzof decision.

While it is true that under Gerzof, the trier of fact may fashion an equitable remedy while still vindicating the public bidding statutes, providing the public is made shole and suffers no loss as a result of the illegality, it is incorrect that the equitable principal was determined by the degree of wrong committed by the contractor.

As the Court held in Gerzof v. Sweeney (p.304):

> "The restrictions imposed by such legislation...[the competitive bidding statutes]...are designed as a safeguard against the extravagance or corruption of officials as well as against their collusion with vendors" (emphasis added).

As the Court stated, the statutes are designed to protect against the extravagance of officials and not merely their collusion with corrupt vendors.

In Gerzof the Court found that the contractor was not an "innocent victim" but a willing participant in the violation of the bidding statutes. Yet the Court fashioned an equitable remedy. Its decision could not therefore have been based on the guilt or innocence of the contractor.

The Court stated its reason for creating an equitable remedy and foregoing complete forfeiture in Gerzof when it said, at page 305, that:

> "...the sheer magnitude of the forfeiture that would be suffered by the defendant...as well as the corresponding enrichment that would enure to the Village of Freeport... adds an element to this case not to be found in any of those in which the principles we have been discussing have been applied" (emphasis added).

The basis for the creation of an "equitable" remedy in Gerzof was not the guilt or innocence of the bidder but the "magnitude of the forfeiture and corresponding enrichment", elements not found in the instant action.

In the instant action should the decision of the District Court stand it would be the public which would suffer a loss in disregard of the public policy of the State of New York and the applicable law as set forth in the Gerzof decision.

In Gered the New York Court of Appeals stated:

> "We have constantly held, primarily on public policy grounds, that, where the City fathers have deviated from the statutory mode for the expenditure of funds and letting of contracts, the party with whom the contract was made could not recover..."

The Court placed no import upon the guilt or innocence of the contractor. In fact, the Court held that collusion on the part of the bidder should not affect this policy when it added:

> "The result should not differ where the due administration of the bidding statute is interferred with and competitive bidding thwarted by the unlawful collusion of the bidders themselves, resulting in a gross fraud upon the public."

Moreover, Judge Fuld, in reaffirming the New York Rule that in order to preserve the sanctity of the public bidding statutes a contractor who is party to an illegal contract must be punished for his participation regardless of his culpability or the misconduct of public officials involved stated:

> "We may adopt this course, in the usual circumstances of the present case, [the magnitude of forfeiture as well as corresponding enrichment] without disturbing the salutory rationale and policy underlining such decisions as Albany Supply and Equipment Co. v. City of Cohoes ..." (at page 304).

The underlying policy of which Fuld speaks is that the public must suffer no damages as a result of the illegal contract.

POINT V

THE TRIAL COURT ERRED IN EXCLUDING EVIDENCE OF STATE ACTIONS BROUGHT BY PRIME CONTRACTORS AND SUBCONTRACTORS AGAINST THE BOARD.

AETNA states (Aetna's Brief, p. 54) that the BOARD has made a totally true and misleading statement in stating that AETNA agreed to assume the obligations to defend the BOARD against prime contractor suits in the supplemental agreement as consideration of the BOARD's forbearance to sue. AETNA asserts that the supplemental agreement is completely devoid of any such statements or representation. (Aetna's Brief, p. 64)

Article 4, subdivision 2 of the supplemental agreement provides (1043a):

> "The contractor hereby agrees to indemnify and hold harmless the Board against any and all claims or causes of action which may be asserted against the Board by either TAC and/or the other Prime Contractors for damages incurred prior to the date of execution hereof by TAC and/or the other Prime Contractors as a result of, or by reason of, any acts or omissions of the Contractor ....."

There can be no question, therefore, but that the supplemental agreement does contain a provision on the part of AETNA to assume the obligations to defend the BOARD against prime contractor suits.

AETNA makes a misleading statement in POINT V of its brief in stating that the subcontractor claims were dismissed as against AETNA in the State courts. Although the actions have been dismissed as between AETNA and the subcontractors, the BOARD as yet has not brought AETNA into these proceedings as third-party defendants under their surety contract. It is AETNA's responsibility under the surety contract which has not been determined.

The Trial Court was incorrect in excluding the alleged claims by prime contractors. The BOARD does not seek monetary damages from AETNA on these claims, but has merely requested a ruling that the contractor and bonding company are responsible for the defenses of the related State actions brought against the BOARD.

Not only has AETNA agreed in the supplemental agreement to assume the obligations for the defense of the BOARD in these actions but, moreover, under the rule of the State of New York that the public may not suffer damage as a result of the illegal contract, the Court must hold FABRIZIO and AETNA responsible for any damages recovered against the BOARD in the various State actions.

Although the results in those State actions may be speculative, the true measure of damages suffered by the public will only be determined by the actual cost to the public for the completion of the work on the school.

Had there been no illegality, there would have been no damage. The BOARD should have been permitted to introduce evidence to show that the actions brought by the Prime Contractors and the Subcontractors are a direct consequence of the illegal contract between FABRIZIO and the BOARD.

AETNA's assertion (Aetna's Brief, p. 66) that the Trial Court found that the delays caused on the project were the fault of the BOARD has no basis in fact. The Court found that disputes arose almost immediately after construction began. The Court did not find, however, that any delays on the project were the fault of the BOARD, nor did the Court state anywhere in its opinion that the actions of the BOARD caused delays which are now the subject of the State Court actions.

That the Court, in fact, committed reversible error in that it did not permit the BOARD to introduce evidence of the State Court actions nor in holding the Contractor and AETNA responsible for the defense of those actions.

Dated: New York, New York
This 10th day of September, 1974

Respectfully submitted,

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